

**TOWN OF HARPSWELL, MAINE**  
**Management's Discussion and Analysis**  
**For the year ended December 31, 2006**

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As management of the Town of Harpswell, Maine, we present this narrative to provide you with an overview and analysis of our annual financial statements for the year ended December 31, 2006. This information, in conjunction with the notes to the financial statements, can be considered when reading the Town's financial statements.

**Financial Highlights**

- ❖ Total assets of the Town of Harpswell exceed its liabilities by \$7,812,049. Total assets include the costs of the 2004 capital roads project which was completed in 2006 and progress payments made in 2006 relating the 2006 capital roads project. Total assets exclude the remainder of the Town's infrastructure assets. This infrastructure, primarily roads, will be included in the Town's 2007 financial statements.
- ❖ The Statement of Activities shows an increase in net assets of \$582,073 for the fiscal year. In addition to the 2006 capital road project referred to above which increased net assets by \$262,361, the Town experienced an increase in taxes receivable of \$120,869, resulting from a combination of higher tax rates and slightly less favorable collection rates. The Town also ended the year with higher cash balances as a result of both higher tax rates and higher levels of miscellaneous revenue, primarily interest earned on cash balances, fees generated at the Town's transfer station and revenues from the sale of certain recyclable materials.
- ❖ During 2006, the Town repaid \$365,833 of the principal of its long-term debt and borrowed \$350,000 to fund in part its 2006 capital roads project.
- ❖ The ending fund balance for all governmental funds is \$3,840,111.
- ❖ The ending fund balance for the general fund is \$3,629,180, an increase of \$141,729 over the previous year. Of this balance, \$446,825 is designated for on-going projects. This leaves an undesignated balance of \$3,182,355, which is sufficient for compliance with the Town's Fund Balance Policy. This Policy requires the Town to maintain an undesignated fund balance of 3 times the average of the previous year's monthly expenditures. In addition to its general funds, the Town has a fund designated for capital projects, and two funds for its special revenue activities. During 2006, the fund designated for capital projects increased from \$18,997 to \$155,625 as the 2004 capital road project was completed and the 2006 was partially completed.

**Overview of Financial Statements**

The Town of Harpswell's basic financial statements are comprised of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also contains other supplemental information in addition to the basic financial statements.

**Government-wide Financial Statements**

The *government-wide financial statements* provide a broad overview of the Town of Harpswell's finances, in a manner similar to private-sector business. Financial information is presented in two statements – *statement of net assets* and *statement of activities*.

The *statement of net assets* presents information about the Town's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Town is improving or deteriorating.

The *statement of activities* presents information about how the Town's net assets have changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the Town of Harpswell that are principally supported by taxes and intergovernmental revenues. The governmental activities of the Town of Harpswell include general government, public works (roads, solid waste disposal), protection and safety (law enforcement, fire protection), health and welfare, culture and recreation, debt service and capital planning expenses.

**TOWN OF HARPSWELL, MAINE**  
**Management's Discussion and Analysis, Continued**

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**Fund Financial Statements**

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Town of Harpswell, like other state and local governments, uses fund accounting to insure and demonstrate compliance with finance-related legal requirements.

**Governmental funds** are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the Town's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds and governmental activities*.

The Town of Harpswell maintains four individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund. Data from the four governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of *combining statements* elsewhere in the report.

The Town of Harpswell adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

The basic governmental fund financial statements can be found on pages 15-16 of this report.

**Notes to the financial statements.** The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 19-30 of this report.

**Other information.** The combining statements referred to earlier in connection with non-major governmental funds are presented immediately following the notes to the financial statements. Combining and individual statements and schedules can be found on pages 33-43 of this report.

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**Management's Discussion and Analysis, Continued**

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***Statement of Net Assets Information***

The following information is a condensed version of the Statement of Net Assets.

<b>Town of Harpswell Net Assets</b>			<b>Governmental Activities</b>	
			<b>2006</b>	<b>2005</b>
<b>Assets:</b>				
Current & other assets	\$	4,135,835	\$	3,740,607
Capital assets		6,124,734		5,884,362
<b>Total Assets</b>		<b>10,260,569</b>		<b>9,624,969</b>
<b>Liabilities:</b>				
Long-term debt outstanding		(2,310,834)		(2,326,667)
Other liabilities		(137,686)		(73,082)
<b>Total Liabilities</b>		<b>(2,448,520)</b>		<b>(2,399,749)</b>
<b>Net Assets:</b>				
Invested in capital assets, net of debt		4,167,025		3,909,495
Restricted		181,435		26,767
Unrestricted		3,463,589		3,288,958
<b>Total Net Assets</b>	<b>\$</b>	<b>7,812,049</b>	<b>\$</b>	<b>7,225,220</b>

The Town's Total Net Assets increased by \$582,073 during 2006. Increases in assets of approximately \$635,000 were offset by increases in liabilities of approximately \$ 49,000. Asset increases included increases in cash balances resulting from higher levels of interest income and certain other non-property tax revenues. Taxes receivable also increased as a result of a higher tax rate and a slightly decreased collection rate. Capital Assets increased as a result of the Town's 2006 capital road project.

Long-term Debt obligations decreased during 2006 by \$15,833 as scheduled principal repayments were offset by a new borrowing in the amount of \$350,000 for the 2006 capital road project.

53% of the Town's Net Assets at December 31, 2006 is represented by its capital assets less any debt outstanding that was used to acquire those assets. Although the Town's investment in capital assets is reported net of related debt, the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

A small portion of the 2006 Net Assets is restricted for Capital Projects, grants and recreation programs. The increase during 2006 reflects the 2006 capital road project which has been only partially completed.

Unrestricted Net Assets includes amounts designated to be expended for certain purposes in subsequent years.

**TOWN OF HARPSWELL, MAINE**  
**Management's Discussion and Analysis, Continued**

***Statement of Activities Information***

The following information is a condensed version of the Statement of Activities.

**Town of Harpswell**  
**Changes in Net Assets**

	<b>Governmental Activities</b>	
	<b>2006</b>	<b>2005</b>
Revenues:		
Program Revenues:		
Charges for services	\$ 235,933	\$ 227,394
Operating grants & contributions	122,926	134,374
General Revenues:		
Property and excise taxes	10,851,395	10,625,102
Subsidies, grants & entitlements	237,718	266,974
Interest earned	123,474	49,512
Other	248,850	466,527
Total revenues	\$ 11,820,296	\$ 11,769,883
Expenses:		
General government	1,193,679	1,114,356
Public works	863,947	834,654
Protection and safety	683,886	629,084
Health and welfare	26,119	28,783
Culture and recreation	247,847	238,216
Education	6,998,238	6,714,259
County taxes	840,931	739,377
Overlay/abatements	70,049	67,035
Interest on long-term debt	144,372	131,082
Capital and special projects	169,155	237,915
Total expenses	11,238,223	10,734,761
Change in net assets	582,073	1,035,122
Net assets, beginning of year, as restated	7,229,976	6,190,098
Net assets, end of year	\$ 7,812,049	\$ 7,225,220

**Governmental Activities**

Governmental activities increased the Town's net assets by \$582,073. Total program revenues were essentially flat on a year to year basis, as small increases in charges for services were offset by decreases in grants and contributions. In the public works area, revenues increased by approximately \$16,000. Fees generated at the transfer station increased as a result of increased volumes. Sales of recyclable materials benefited from higher prices on metals and newspaper. Finally, sales of reclaim and wood chips were at higher levels in 2006 than 2005. Offsetting these increases was a \$6,000 decrease in recreation fees attributable to a change in the scheduling of the department's ski program. With respect to operating grants and contributions, the State of Maine continued to decrease its support of programs in the areas of small community grants and grants for overboard discharge. Reimbursements from the State of Maine relating to the Town's general assistance program decreased as the Town experienced a decrease in requests under this program.

Property tax revenue increased as the property tax base expanded. Revenue sharing funds received from the State of Maine continued to decline. Interest earned increased as a result of higher average balances and a higher interest rate. The decline in other revenues largely reflects the donation in 2005 of \$282,700 in land and buildings at Mitchell Field.

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**Management's Discussion and Analysis, Continued**

To aid in the understanding of the Statement of Activities, some additional explanation is provided. Please note that the format differs from that of the Statement of Revenues, Expenditures, and Changes in Fund Balance. Expenses for each activity are listed in the left-most column with revenues generated by that particular activity reported to the right. Subtracting one from the other results in a Net (Expense)/Revenue. This format provides information about the relative financial burden on the Town's taxpayers of each activity. It should be noted, however, that while these revenues may be generated by specific activities, the Town does not have dedicated revenue sources. Accordingly, revenues from specific activities are deposited to the Town's general fund, as are all tax payments received. From this fund, the Town makes all its expenditures.

Examples of activities which produce some level of revenue are:

<i>Public works</i>	Transfer Station fees and recycling revenues Local Road Assistance
<i>Health and welfare</i>	General Assistance state reimbursement
<i>Cultural and recreational</i>	Fees for recreation programs
<i>Capital and special projects</i>	Grants for restricted projects

All other governmental revenues are reported as general revenues. It is important to note that all taxes are classified as general revenue, even if restricted for a specific purpose.

***Net Cost of Governmental Activities***

The following information is a breakdown of each of the Town's major functional activities.

**Town of Harpswell**  
**Net Cost of Governmental Activities**

	<b>Total Cost of Services</b>		<b>Net Cost of Services</b>	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
<b>Function / Program</b>				
General government	\$ 1,193,679	\$ 1,114,356	\$ 1,193,679	\$ 1,114,356
Public works	863,947	834,654	617,398	603,364
Protection and safety	683,886	629,084	683,886	629,084
Health and welfare	26,119	28,783	22,319	21,191
Culture and recreation	247,847	238,216	213,163	196,812
Education	6,998,238	6,714,259	6,998,238	6,714,259
County taxes	840,931	739,377	840,931	739,377
Overlay/abatements	70,049	67,035	70,049	67,035
Interest on long-term debt	144,372	131,082	144,372	131,082
Capital and special projects	169,155	237,915	95,329	156,433
<b>Total governmental activities</b>	<b>\$ 11,238,223</b>	<b>\$ 10,734,761</b>	<b>\$ 10,879,364</b>	<b>\$ 10,372,993</b>

Total Cost of Services and Net Cost of Services increased from 2005 to 2006 by 4.69% and 4.88%, respectively. Most of these increases results from the increased assessments made by MSAD #75 and by Cumberland County, which in turn reflect the increase in the Town's valuation. Interest on long-term debt increased as a result of amounts borrowed on a short-term basis in 2006.

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**Management's Discussion and Analysis, Continued**

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## **FINANCIAL ANALYSIS OF THE TOWN'S FUNDS**

As of December 31, 2006, the Town's governmental funds balance totaled \$3,840,111.

As noted earlier, the Town uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The financial performance of the Town as a whole is reflected in its governmental funds.

**Governmental funds:** The focus of the Town's governmental funds is to provide information on near-term inflows, outflows, and balances available for spending. Governmental funds report the differences between their assets and liabilities as fund balances. Reserved amounts reflect that which is not available to be spent while undesignated amounts reflect amounts that are.

## **GENERAL FUND BUDGETARY HIGHLIGHTS**

The Town's General Fund fund balance increased 4% from \$3,487,451, as restated, in 2005 to \$3,629,180 in 2006. The increase of \$141,729 in the 2006 General Fund fund balance was attributable to actual revenues exceeding expenses by \$345,583 plus a \$3,401 transfer from grants, less the use of \$200,000 for the 2006 capital roads project and \$7,255 for recreation programming. In addition, \$204,000 of undesignated fund balance was approved by the 2006 Town Meetings to be used for the following purposes: \$150,000 to reduce the tax commitment, \$50,000 to fund the withdrawal process from MSAD # 75, and \$4,000 for a salary survey of elected positions. Consistent with the Town's policy of maintaining three months of expenses in its year-end General Fund fund balance, the 2006 year-end level will allow use of \$250,000 in 2007 to reduce the tax commitment and to fund a capital reserve set aside account.

**Revenues.** During 2006, the Town benefited from favorable interest rates and higher average balances to the extent that interest earnings were up 149% from the prior year (\$49,512 to \$123,474). Transfer Station fees and sales of recycled materials continued to generate significant revenue. The total of these revenues increased 18% due to receipt of slightly higher volumes at the Transfer Station and improved market prices for scrap metal and recycled newspaper. In 2006 the Town levied one of its largest fines for a land use violation in the shoreland zone which amounted to \$20,000. In the aggregate, fees generated 19% more revenue than anticipated, primarily in the areas of building and plumbing permits, Planning Board applications, moorings registrations and late registration of dogs. The highest single source of non-property revenue, the excise tax, remained relatively flat as the rising price of gas contributed to lower demand for new or expensive vehicle models which traditionally generates a greater annual increase in excise revenue than what was experienced between 2005 and 2006. Also, as predicted, the Town received less Revenue Sharing from the State of Maine (\$169,969 in 2006 compared to \$202,629 in fiscal year 2005) as more of that revenue stream is provided to service center communities.

**Unexpended Appropriations.** Notable unexpended appropriation lapses to the 2006 general fund occurred in the areas of general government, assessing, legal, planning, recycling, harbormaster, and shellfish operations. With respect to general government, the 2006 budgeted appropriation contemplated a Deputy Town Administrator being hired in the beginning of the second quarter. Ultimately, the position was filled in late August. The budgeted part-time position in assessing was able to be covered by the current Codes Enforcement Officer secretary and therefore those funds did not need to be expended. General legal expenses were controlled because the Town did not have to defend itself against a lawsuit in 2006. In the one case of litigation where the Town brought suit, all legal fees were covered by the defendant pursuant to the settlement agreement. With regard to planning, the Town deferred selection of a consultant for the Mitchell Field Planning process and will carry forward \$5,000 for those services in 2007. With volumes remaining relatively flat at the Recycling Center and Transfer Station, anticipated increases in disposal costs were not incurred. The Harbormaster did not find it necessary to move a major number of moorings in Mackerel Cove as had been anticipated and therefore the Town did not need to expend those funds. Finally, due to the changeover of personnel relative to marine patrol, Cumberland County refunded the Town \$15,000 because it was unable to provide the contractual coverage that the Town expected.

**Overlay.** As there were still many abatement cases in process that related to the 2005 revaluation, the Town budgeted \$164,673 in overlay, expended \$70,049 with the remaining \$94,624 lapsing to the general fund.

**Contingency.** The use of contingency was relatively limited in 2006. There were only three areas of the 2006 budget that exceeded appropriated amounts: (1) \$9,875 to complete Field Road which was part of the 2004 Capital Road

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**Management's Discussion and Analysis, Continued**

Reconstruction Project; (2) \$187 to cover the general law enforcement contract with Cumberland County and (3) \$3,703 to pay for advance life support intercept services provided by Midcoast Hospital in Brunswick.

Harpswell maintains a healthy General Fund fund balance fund balance that is used to fund first quarter expenditures until such time as a tax anticipation note is needed to fund expenditures up to the time when property tax revenue is collected.

The annual Town Meeting, which is held in March of each year, votes on the budget as recommended by the Selectmen for the upcoming year.

**CAPITAL ASSET AND DEBT ADMINISTRATION**

***Capital Assets***

At the end of 2006, the Town had \$6,137,966 net investment in capital assets (excluding infrastructure invested in before 2005), and outstanding debt of \$2,310,834. \$197,500 of the outstanding debt was borrowed to finance Town-wide revaluations in 1997 and 2004, and to contribute to the Harpswell Heritage Land Trust. The remainder of the debt was borrowed to acquire, build or renovate land, buildings and equipment at the Town offices and the Town's solid waste facility.

**Town of Harpswell**  
**Capital Assets, net of depreciation**

	<b>Capital Assets</b>		<b>Accumulated Depreciation</b>		<b>Capital Assets, net of depreciation</b>	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
Land	\$ 1,980,461	\$1,980,461	\$ -	\$ -	\$1,980,461	\$ 1,980,461
Construction in progress	262,361	560,658	-	-	262,361	560,658
Buildings and building Improvements	4,023,632	4,023,632	(1,127,348)	(993,176)	2,896,284	3,030,456
Equipment and furniture	594,662	618,249	(313,587)	(305,462)	281,075	312,787
Infrastructure	711,669	-	(7,117)	-	704,552	-
<b>Total capital assets</b>	<b>\$ 7,572,785</b>	<b>\$7,183,000</b>	<b>\$ (1,448,052)</b>	<b>\$ (1,298,638)</b>	<b>\$6,124,733</b>	<b>\$ 5,884,362</b>

During 2006, the Town completed its 2004 capital road project at a total cost of \$711,669. At the end of 2005, progress payments relating to this project which totaled \$560,658 were included in construction in progress. The Town undertook a new capital roads project in 2006, \$413,372 was expended in 2006 and \$262,361 remained in construction in progress at year-end. There were no other significant additions to capital assets during the year.

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

The Town of Harpswell is predominantly a residential and seasonal community. The Town does not have any significant commercial or industrial sector to support the cost of municipal government. The presence of a large number of seasonal homes, most of which are owned by nonresidents, provides a significant source of property tax revenue for the Town. This benefit, however, is counterbalanced by the Town's high total property valuation which has a major effect on its share of the M.S.A.D. # 75 budget and that of the Cumberland County budget as well.

Despite the planned closing in 2011 of Brunswick Naval Air Station, which is located in an adjacent community, the regional economy at this time appears relatively strong with major retail development continuing to occur at a rapid rate in Topsham and Brunswick. The announcement of the military base closure has not had a drastic effect thus far on real estate values in Harpswell, particularly the waterfront market which continues to command high prices. However, the softening of the housing market nationally and regionally (New England and Maine) appears to be slowing down the rapid rate at which housing prices have been escalating which will ultimately reduce the rate at which overall property values of the Town will increase.

## **ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES, CONTINUED**

Due to continuing dissatisfaction with Harpswell's share of the M.S.A.D. # 75 budget, voters approved, in late January of 2006, the creation of a statutory Withdrawal Committee that negotiated with M.S.A.D. # 75 on the terms of an eventual withdrawal. The Harpswell Withdrawal Committee submitted a proposal to the Commissioner of Education that was rejected because the proposal had not been reached in agreement with M.S.A.D. # 75. Subsequently, the Selectmen received a citizen-initiated petition calling for the withdrawal effort to be terminated.

That item is scheduled to be voted on in March of 2007. In the meantime, the Governor has proposed a major consolidation plan that would put Harpswell in a mandatory school district with the other towns of M.S.A.D. # 75, as well as with Brunswick and Freeport. While the consolidated effort could mean savings to Harpswell, particularly in the area of administration, the details and effects of the Governor's proposal are not well understood or demonstrated at this early stage. In addition, the State's Essential Programs and Services funding model is based on valuation which causes Harpswell to be a minimum receiver of State assistance for education. In fact, it was only because of special legislation enacted in 2006 that Harpswell will continue to receive State reimbursement for its special education costs. Because educational costs impact property taxpayers so significantly, the Town intends to monitor school consolidation proposals and the potential effects on Harpswell taxpayers.

2006 was the first year that the Town of Harpswell was constrained by the LD-1 legislation which caps the amount of property tax that can be collected to fund budgets, including the municipal budget. The 2006 municipal budget did not exceed the levy limit established for Harpswell; however, it is anticipated that in 2007 voters will be asked to increase the property tax levy limit. There are primarily two new items in the proposed 2007 budget that may cause the LD-1 limit to be exceeded: (1) \$50,000 for the Holbrook Foundation to preserve a working waterfront in Cundy's Harbor and (2) \$135,000 for a Brush Truck to assist the Town with its emergency services operations. By being less conservative in its practice of estimating revenues, the Town will budget approximately \$135,000 more of estimated revenues in the 2007 budget to reduce the amount of property tax that needs to be collected. The 2007 estimated revenues correlate closely to 2006 actual revenues.

The State legislature created a Working Waterfront Program that provides tax relief to certain qualified property owners of working waterfronts in Maine. Program details have just been released. The Town's early impressions are that penalties associated with the program are so severe that it is unclear how many Harpswell property owners may avail themselves of this program. Therefore it is unknown what the resulting impact on the tax rate might be.

Budget development is always predicated on a concern that not all residents of the Town have incomes that keep pace with the rate of property valuation. It is anticipated that the 2007 municipal budget will increase approximately 9% from the prior year. The State's special education reimbursement for Harpswell in 2007 (which is likely to be upwards of \$700,000), however, is expected to keep the Town's obligation to M.S.A.D. # 75 down. Because of this circumstance, 2007 is a year in which it is expected that the 9% municipal increase could be absorbed without a significant impact on the mill rate. As currently constructed, the proposed 2007 municipal budget will require voter approval to increase the LD-1 levy limit imposed on Harpswell in 2007. By using reasonable revenue estimates in 2007 and proposing the use of \$250,000 of undesignated fund balance, the extent to which the levy limit imposed by LD-1 may need to be increased is limited.

## **CONTACTING THE TOWN'S FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of the Town's finances and to show the Town's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Selectmen's Office at P.O. Box 39, 263 Mountain Road, Harpswell, Maine 04079-0039 or by phone at (207) 833-5771.